USAID Policy Paper

Shelter

Bureau for Program and Policy Coordination
U.S. Agency for International Development
Washington, D.C. 20523

February 1985

Shelter Policy Paper

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PREFACE

This Shelter Sector Policy supersedes PD-55, "Shelter Program Objectives" approved on October 24, 1974. This revision reflects the additional experience USAID has gained since then, in responding to the shelter requirements of the LDCS. This policy statement also describes the forms of assistance which may be available for financing shelter projects and sets out the criteria for determining the most appropriate form for individual developing countries. The primary vehicle has been the Housing Guaranty (HG) program. The HG projects are often supplemented by DA or ESF financed capital and technical assistance concerning housing policy formulation, institutional development and training, and the introduction of appropriate technologies in the form of innovative housing design, and support for the private sector as the main vehicle for the delivery of shelter.

EXECUTIVE SUMMARY

The Shelter Context

Spontaneous shelter activities are high on individual priority lists. People throughout the world will invest personal time and energy in the construction and improvement of their own homes. Experience has proven this to be as true in the upgrading of reed huts to tin and ultimately to brick, as it is in the "do-it-yourself" construction activities of developed countries. It is USAID's policy to take account of and encourage these private energies. They act as a "multiplier effect" on official inputs.

Shelter is a basic human need, following the need for food and clothing. Most LDCs recognize shelter as a priority in their development strategies because it is a basic aspiration of their people.

- Investment in the shelter sector represents the largest capital investment in urban centers. Therefore, shelter policies, planning, and programs which are efficient, affordable, and seek maximum cost recovery are important components of national economic development and urban policy.

- Shelter is one of the highest priorities of low-income households. It represents a household's largest capital asset and is a major stimulus to individual saving.

- Shelter contributes to national economic growth objectives directly, through its stimulation of the construction and building materials sector, and indirectly through the furniture and household products industries. It provides jobs for large numbers of unskilled labor. Shelter construction by the formal and informal private sector accounts for the overwhelming portion of new shelter produced in developing countries.

USAID's Shelter Sector Objectives

USAID's shelter sector objectives recognize the relationship of shelter to overall economic development and to the basic priorities of the Agency. They are to:

- Assist in the formulation of rational housing policies.
- Demonstrate the feasibility of shelter solutions poor families can afford.
- Facilitate mobilization of additional local resources for financing shelter.
- Develop sustainable shelter and urban service institutions.
- Increase participation of the private sector, including the informal sector.
- Encourage the use of energy and resource efficient housing designs, technologies and standards consistent with the objective of producing shelter which is affordable.
- Increase the survival rate of people and buildings in disaster prone areas through adoption of appropriate zoning and building regulations.

The overwhelming portion of annual additions to the LDC shelter stock is the product of the effort and energy of the informal private sector. Any shelter program with the goal of meeting minimum shelter needs must acknowledge, facilitate, and support these informal sector efforts.

While significant, the shelter needs of a developing country are solvable within a finite period if realistic and affordable minimum housing standards are established, and appropriate financial policies adopted. Analyses undertaken in a number of countries have shown that basic shelter needs can be satisfied with a marginal increase in national investment, if realistic design standards and financial policies are adopted.

The magnitude of the shelter sector requirements of LDCs far exceeds the resources available from USAID Therefore, it is essential that USAID resources for shelter be fully exploited as a catalyst to help the LDCs mobilize their own resources for shelter and to use them more efficiently equitably. It is also important to coordinate our technical and capital assistance with that of other donors to the greatest extent possible.

USAID's shelter programs must benefit, directly or indirectly, households below the median income level of the country or city of concern.

Programs to meet USAID's objectives can include: provision of access to secure land tenure for low-income groups; modification of inappropriate building standards which unnecessarily result in structures that poor families cannot afford; strengthening of weak institutional structures; modification inappropriate interest rates; reduction of direct or direct subsidies for housing; and emphasis on objectivity of shelter decision by government.

Forms of Assistance Appropriate for Shelter Projects

Shelter programs should be based on justification in a Country Development Strategy Statement (CDSS). Shelter projects are appropriate for financing with DA, ES dollars, PL 480 and FAA generated local currencies in all countries. USAID will continue to be sympathetic to requests for assistance for reconstruction of shelter in countries struck with earthquakes or floods, or other disasters. DA or ESF fund may be used for such disaster relief as appropriate to the individual country situation, if adequate PL 480 or FAA generated local currency is not available.

Country eligibility for Housing Guaranties (HG) will be based upon the judgment of the Mission, ME, the regional bureaus, an PPC upon an analysis of the sectoral, economic, and political feasibility of the proposed program. A thorough analysis of the debt servicing capability and record is required for every candidate in order to identify borrowers with doubtful prospects for meeting their loan servicing obligations on schedule. This risk analysis must be under taken early in the project development process and any issues identified and resolved the first stages of project preparation. One reason for applying credit worthiness standards to HG loans is to enhance the prospect of timely debt service performance an in this way minimize drawdowns of the reserve fund.

As a general principle, market rate HG loans are not an appropriate form of development assistance for very poor countries. Therefore, countries which receive IDA credits, but not IBRD loans, may receive HG loans only after special justification for the exceptional country is approved by the Assistant Administrator of the Regional Bureau concerned, and the Assistant Administrator for PPC or by the Administrator.

Characteristically, very poor countries, as defined above, have shallow resource bases. Consequently, the prospects are slim for sustained improvement in their export earnings relative to their minimum import need. In order not to jeopardize their long term development hopes, these countries must exercise caution in mortgaging their prospective export earnings. These countries must examine carefully both the terms of their foreign borrowings and the purposes for which such debts are incurred. The thirty year life and the ten year grace on principal repayments of the typical HG loan are advantageous, but the near commercial interest rate is not appropriate for the world's poorest countries. In ranking competing needs for the small volume of nonconcessional foreign loans very poor countries can afford to service, priority over shelter projects must be given to financing the essential imports requirements of highly productive investments which will improve the economy's trade balance and its foreign debt servicing capabilities. Shelter projects require few imports (typically less than ten per cent of the total cost). Hence they can be financed largely with local resources. They will not improve the debt servicing capability of the borrower. Therefore, shelter projects merit low priority in the competition for foreign loan resources.

USAID SHELTER POLICY PAPER

I. INTRODUCTION

"USAID's goal in the shelter sector is to assist LDCs to develop the institutional, technological, and financial capacity to provide shelter under reasonable conditions for all levels of society, with emphasis on government actions to meet the needs of the poor." This opening sentence from the PD-55, "Shelter Program Objectives", October 22, 1974, still summarizes the overall objective of the Agency. However, in the nearly ten years which have gone by since this last Shelter Policy Paper, USAID has gained substantial experience with shelter programs and projects. It is, therefore, appropriate to redefine USAID's Shelter Sector Policy in light of this experience and changing conditions.

For over 20 years, USAID has made an important contribution to understanding and designing solutions to the shelter problem of the LDCS. The vehicle has been capital provided through the HG program in combination with grant-financed technical assistance in housing policy formulation, institutional development and training, and the introduction of appropriate technologies in the form of innovative housing designs. USAID has been a pioneer of the sites and services and settlement upgrading concepts and support for the private sector as the main vehicle for the delivery of shelter.

During this 20-year history, USAID through the HG Program, has undertaken 152 projects in 44 developing countries with over one billion dollars in disbursements and $1.5 billion in authorizations. Among donor countries, the United States provides the largest amount of assistance to the shelter sectors of developing countries through the HG program.

II. THE SHELTER SECTOR CONTEXT

Shelter is a basic human need, following the need for food and clothing. Most LDCs recognize shelter as a priority in their development strategies, because it is a basic aspiration of their people and it is an essential component for sustained national economic growth.

Shelter provides essential contributions to overall national economic development which, when combined with its social benefits, justifies a claim on an appropriate level of national and international resources in relation to investment in other sectors. In this sense, shelter and infrastructure contribute toward making investments in other sectors, such as industry and agriculture, more productive. A minimum level of shelter is essential to productive workers.

Well located and designed shelter and urban services and facilities are an essential part of the productive investment base of any modern economy and contribute to the efficiency and productivity of national development programs.

The supply of shelter is critical to the orderly growth of urban areas. Shelter represents a significant share of overall urban investment from both public and private sources. Typically, the informal sector has provided 80 percent of the existing housing stock, without the benefit of formal lines of credit. The efficiency and productivity of this informal investment is of critical importance to individual households as well as to national development.

Shelter and urban services and facilities create demand within the domestic construction and building materials industries. A dynamic construction industry is essential for overall national development. Shelter construction, both formal and informal, can provide major stimulus to the development of skills, entrepreneurship, and the capital investment necessary to make the construction sector a major contributor to national economic growth. It also provides a point of entry into the job market for many unemployed and unskilled workers and can stimulate small-scale and informal private sector contractors.

The maintenance of an adequate supply of well located and affordable shelter contributes to overall worker productivity. The incentive of home ownership can attract otherwise unavailable private savings into the banking system. It contributes to the national capital stock. For most low-income households, home ownership is their most likely means of accumulating capital assets which in turn can be mortgaged to provide working capital for small-scale enterprises and other household economic purposes. Housing contributes to consumer demand for household products and furniture, further strengthening other sectors of the economy.

The scale of the shelter sector challenge in the LDCs is enormous. The United Nations estimates that urban areas in the LDCs will increase by one billion persons between 1980 and 2000. Most of these people will be poor USAID estimates that 300 to 350 million new housing units will be required as replacement stock and to accommodate new household formation, and between 41,000 and 105,000 square kilometers of new land will be urbanized depending on the densities and policies selected. The World Bank estimates that over $600 billion will be required to meet the water supply and sanitation requirements of the expected population growth.

It is apparent that the selection of appropriate policies, interest rates and standards, the pursuit of cost recovery mechanisms, the mobilization of private savings for investment in shelter, the coordination with other donors, the appropriate distribution of responsibilities between the public to the private sectors, and the efficiency of both the formal and informal shelter sector delivery systems can have a major impact on the ability of LDCs to meet the enormous challenge of urban growth. USAID, through its shelter sector programs, can do much to assist LDCs to meet the challenge with technical assistance, training, and selected capital assistance through the Housing Guaranty mechanism.

USAID's research studies, now in process or being further developed, show that most shelter sector needs of LDCs can be met through the adoption of appropriate policies, affordable standards, and private resource mobilization without adversely effecting other development sectors.

III. FRAMEWORK FOR DEVELOPING SHELTER STRATEGIES

In seeking to improve the physical living conditions of its people, the typical developing country is confronted with a series of difficult problems. In assessing a proposed Shelter program for any country, the Mission should make a judgment on whether its economic policy orientation is consistent with reasonable expectation. Policy dialogue objectives should be considered as part of a shelter strategy. Typical problems to be reviewed include:

1. Difficult National Economic Conditions

Inflation, unrealistic interest rate policies, excessive levels of subsidies, low levels of income and employment, and inadequate know-how impede investment in and overall production of shelter. As a component of the development strategy for an individual country, USAID's involvement in shelter programs can help address some of these economic problems and thereby influence the productivity of domestic savings invested in shelter.

2. Politically Charged Approach to Shelter Problems

The combination of limited economic resources, the rising expectations of populations in developing countries, and competition between interest groups, make many aspects of development the subject of vigorous political debates. Shelter is no exception. USAID may help LDCs to avoid the sacrifice of long-term goals in shelter development for short-term political expediency by maintaining a continuous policy dialogue with host country officials, and encouraging the long-term support for technical personnel and the private sector.

3. Limited Access to Urban Land and Secure Tenure

Inappropriate urban land policies often contribute to increased land costs to the urban poor, inefficient land use, and increased infrastructure and service costs. Unclear tenure inhibits urban development and limits access of households to more formal lending institutions. Development of simplified procedures to assist in evaluation of satisfactory mechanisms for determining and transferring title are vital to a healthy residential land market.

4. Inappropriate Physical Development Standards

The legal standards for physical development of housing units and related urban services and facilities are often too high and therefore too expensive for the majority of the urban population to afford. Since low-income housing is very often built by the occupants themselves, such standards affect low-income groups adversely. Greater inequities in the shelter delivery system are the result. An example is the denial by the government of urban services to self-built homes which are below prevailing legal standards.

5. Limited Institutional Capacity

The process of development is frequently hampered by the limited institutional capacity of the host country. Shelter policies and programs, even when well designed, may fail due to the lack of skilled professional personnel, inefficient procedures, dearth of basic data to formulate appropriate policy decisions, and the lack of coordination among various agencies responsible for implementing aspects of a shelter program.

6. Failure To Maximize Private Savings

Many LDCs have not yet developed the financial policy framework or institutional structure necessary to mobilize adequate private savings for shelter sector investment. About 80 percent of shelter finance is currently provided through informal channels. The remainder is supplied through formal credit institutions which generally serve middle and upper-income groups. While international transfers, such as the HG program cannot substitute for domestic savings mobilization, they can be used catalytically to assist in mobilizing domestic savings.

7. Inappropriate Interest Rate Policy

Host government policies often hamper the mobilization of indigenous financial resources which might otherwise be available for shelter. Ceilings imposed by the government on interest and/or below the reasonably expected rate of inflation (so as to make them negative in real terms), discourage the flow of investment funds into home finance institutions and often lead to their ultimate decapitalization.

8. Excessive Subsidies

The needs of the developing countries for shelter are vast compared to the availability of resources for meeting them. Therefore, the prerequisite for any successful housing policy addressing the needs of the poor majority is recognition by the government concerned that programs dependent on public subsidies can only make a small dent in the huge need for improved shelter. Their only realistic goal is to undertake shelter construction at standards which are to be affordable by poor families without the necessity for subsidies. The pre-conditions for self-sustaining programs on a scale large enough to have an appreciable impact on shelter requirements include sound pricing policies and cost recovery. Public housing programs often produce housing units that either require recurrent annual subsidies, which exceed the resources available and compound their budgetary difficulties, or produce completed units which are too expensive for low-income households.

9. Inadequate National Housing Policies

Solutions to all of the above problems are made more difficult in the absence of a clear, consistent national housing policy. However, many LDCs do not have explicit housing policies in place. Unfortunately, many of those which do exist are seriously deficient. They frequently do not adequately address the shelter needs of the urban poor, fail to recognize the potential contribution of the informal sector to shelter delivery, do not provide sufficient incentives and opportunities for the private sector to fully participate in all aspects of the shelter sector, and do not reflect the linkage between shelter investment and economic growth.

IV. USAID's SHELTER SECTOR OBJECTIVES

USAID's shelter sector objectives recognize the relationship of shelter to the overall priorities of the agency: policy reform, institutional development, private enterprise development, and technology transfer. In the shelter sector, these Agency priorities address the basic problems faced by most LDCs in striving to improve the physical living conditions of their people and reflect the expertise and the 20-year experience of USAID

The objectives of USAID's shelter programs are to:

1. Assist in the formulation of rational housing policy:
   to encourage the preparation and implementation of national housing policies that reflect USAID's basic objectives and that provide an internally consistent framework for future housing activities.

2. Demonstrate the feasibility of shelter solutions poor families can afford:

to promote the selection of appropriate physical standards, building codes, technologies which will help low-income families gain access to secure land tenure, basic services, and housing.

3. Facilitate mobilization of additional local resources for financing shelter:
to adopt interest rate policies which reflect the real cost of capital, to develop viable institutional systems for financing shelter and urban development, and to minimize the need for public subsidies.

4. Develop sustainable shelter and urban service institutions:
to develop production and delivery capabilities commensurate with the needs of the population with special emphasis on meeting the shelter needs of the urban poor; encourage appropriate user fees, cost accounting and cost recovery for utility expansion to facilitate more rapid expansion of these services.

5. Increase private sector participation:
to encourage and facilitate an increased role for both the formal and informal private sector, including cooperatives and other self-help institutions and credit institutions oriented to the homeowner and home improvement credit, in low-income shelter financing, production and delivery and to achieve an appropriate division of responsibilities between public and private sectors. Government interventions should normally be limited to services which people can not provide for themselves, such as infrastructure. HG assistance should be targeted toward expansion of demand for small contractors and other suppliers, including those in the informal sector. Conversely, support of public sector subsidized housing projects should normally be considered as low priority for USAID funds.

6. Encourage the use of energy and resource efficient housing designs, technologies and standards:
to foster development and application of housing designs that make use of local budding materials as appropriate to the varying regions of the country, that generate on-site utilities (e.g., rainwater collection systems) and that encourage and accommodate kitchen gardens, if appropriate.

7. Increase the survival rate of people and buildings in disaster prone areas:
to discourage development in areas prone to flood, severe storm and earthquake and to encourage adoption of hazard resistant building regulations and codes.

V. USAID's INSTRUMENTS FOR IMPLEMENTING SHELTER PROGRAMS

USAID's shelter sector objectives are to be achieved through joint activities of U.S. USAID Missions, their respective Bureaus, and the Office of Housing and Urban Programs (PRE/H) as defined in Handbook VIII. The following program instruments are available to implement shelter programs:

1. **Shelter Sector Assessments (SSAS)**

For countries where USAID is considering a shelter program, the first step is to conduct a Shelter Sector Assessment in order to obtain an over view of the shelter problems and opportunities. SSAs are designed to identify the problems and policy issues that need to be addressed in the shelter sector as they relate to overall national development objectives and the Mission's Country Development Support Strategy (CDSS). Shelter Sector Assessments are particularly important in those countries where USAID is considering urban programs. PRE/H has prepared a Shelter Sector Assessment methodology designed for this purpose. SSAs have been prepared for most countries in which USAID has carried out Housing Guaranty projects (see Appendix 1). Missions are encouraged to use PRE/H skills and expertise. In countries vulnerable to natural disasters, inclusion of appropriate wind and seismic-resistant features should be examined.

2. **Technical Assistance**

USAID provides both long-term and short-term technical assistance that can contribute to the achievement of shelter sector objectives. Technical assistance is frequently interwoven into the process of preparing and implementing HG loans but can also be provided through grant funds, independent of a capital assistance program. Where country risk of repetitive disasters warrants, assistance may be offered on techniques for reducing vulnerability of the local housing.

Long-term technical assistance involving resident advisers is usually focused on enhancing institutional capacity, improving the shelter delivery systems and financial structure, or the development of housing policies.

Short-term technical assistance frequently involves assistance in project design and implementation, and responding to specific needs and requests from participating country institutions and agencies.

3. **Training**

USAID's shelter training activities are directed toward the development of improved competence and skills in the LDCs, the communication, through training, of USAID's shelter policies and approaches; and the development of a network of shelter professionals and local institutions linked to U.S. and international organizations engaged in implementing shelter programs.

The range of USAID's shelter training activities include annual regional conferences, the annual one month Shelter Sector Workshop, support for university short-courses in shelter-related subjects, support for short-term training at regional institutions in third world countries, and the design and presentation of in-country courses and training seminars. Short-term technical assistance to LDC shelter training institutions can also be provided.

U.S. USAID Missions are encouraged to nominate country participants from the shelter sector to participate in these various training activates.

4. **Research and Information Dissemination**

USAID supports a variety of individual research efforts which have been designed to provide LDC technicians with specific, practical information on innovative approaches to shelter sector issues supportive of its overall objectives. For example, USAID has supported research work on the use of indigenous building materials, building standards and designs, temporary housing for disaster victims, use of bonds and secondary mortgage markets, variable payment mortgages, computer applications in the shelter sector, and analytical case study research and evaluation.

USAID seeks to disseminate information on shelter sector issues and innovative approaches throughout the LDCs through publications, newsletters, and sponsorship and participation in conferences and seminars.

5. **Capital Assistance**

The primary mechanism for USAID capital assistance in the shelter sector is the Housing Guaranty (HG) program. This program was developed as part of the U.S. Foreign Assistance Program in 1961. It is a unique USAID activity in which the U.S. private sector provides long-term financing for low-income shelter and urban upgrading programs in developing countries. (See Appendix I for a full description of the HG program with a U.S. Government guaranty.) If consistent with the country strategy statement, shelter projects are appropriate for financing with DA and ESF resources and PL 480 or FAA generated local currencies in all countries eligible for FAA assistance. Furthermore, USAID will consider sympathetically requests for assistance for reconstruction of shelter in countries hit with earthquakes, floods, or other disasters with whatever resources are appropriate to the individual country's circumstances.

The combination of one of these more concessionary resources with a HG loan has been successfully demonstrated in Zimbabwe, Mauritius, and Costa Rica. It is recognized that USAID capital assistance is no substitute for locally mobilized finance, but it can meet specific important purposes in advancing USAID and LDC shelter objectives. These include:

- Providing assistance toward reaching USAID objectives over time in the broader national development-context. The incremental approach adopted to develop a shelter program, where specific policy objectives are established for each specific loan, provides a forum for on-going policy dialogue and a mechanism to accelerate change.

- Providing capital to create or expand new institutions where necessary and to demonstrate new shelter solutions or programs. Essentially, HG loans assist countries by sharing the risks of innovation and change.

Although the size of any given HG loan must depend on many factors, it is important to recognize that needed change is vastly enhanced by the prospect that a given loan may be part of a continuing series of loans. The series should include mutually agreed policy steps and accelerate problem recognition and design of solutions.

Since HG loans provide untied foreign exchange in excess of the immediate requirements of a particular project, they provide additional foreign exchange resources which can be invested in other productive ventures outside of the shelter sector. In this sense, HG loans can help Missions achieve the broader economic development objectives established for a given country. However, the basic purpose of HG loans is not to provide balance-payments assistance.

VI. TYPES OF SHELTER PROGRAMS APPROPRIATE FOR USAID SUPPORT

The HG Program can be used to finance the following kinds of shelter related programs for families below the median income:

- Slum and Spontaneous Settlement Upgrading: including the legislation of land tenure, provision of potable water, sewerage, electricity, roads, and drainage. Upgrading projects may also include home improvement loans to residents in project areas. These projects are designed to assist families in the informal sector.

- Sites and Services: involving preparation of vacant land for efficient self-help shelter production through subdivision into individual lots and the provision of water, sewer, and other urban services. This type of project may also include training and building materials loans for self-help builders and small-scale contractors. Sites and service projects, therefore, help members of the informal sector reap some of the economic and social benefits of development.

- Core Housing: including a sites and services approach with the addition of a basic housing shell (typically a bathroom and a small multipurpose living area) on each lot, designed to be improved and expanded by the owner. Building materials loans may be provided.

- Low-Cost Housing Units: in special circumstances in middle-income countries, especially when the focus can be on encouraging private sector attention to low-cost housing for the poor population.

- Support for Improvement to Urban Services and Facilities: physical improvements to urban services such as water supply and distribution, sanitation, trash collection, and road and drainage improvements can improve the quality of life in the pre dominantly low-income residential neighborhoods, and foster the development of private enterprise.

- In addition, HG loans can be used to finance schools, health clinics, markets’ job skill training centers, and other community facilities to support the development of neighborhoods; and acquisition of strategic parcels of land to accommodate long-range demand for land for low-cost shelter.

VII. DETERMINATION OF COUNTRIES SUITABLE FOR SHELTER PROJECTS LOANS

1. Country Need for USAID Resources for Shelter

Sectoral issues which would establish a country’s need for USAID assistance include the following:

- Recognition that deficits in shelter and shelter production are adversely affecting economic efficiency and productive potential.

- Reasonable prospects that the LDC will make progress in correcting inappropriate shelter policies, such as the use of unaffordable shelter sector standards, reliance on deep subsidies, or inadequate cost recovery, or other problems that can be usefully ad dressed by USAID programs which will lead to substantial increased efficiency in the utilization of domestic shelter sector resources.

- An assessment of the LDC’s need and willingness to increase the mobilization of sufficient domestic savings to support essential shelter production. The identification of opportunities for enhancing the private sector’s role in the shelter sector. The determination that USAID’s shelter sector initiatives will be supportive of the overall USAID country strategy and the LDC’s national development objectives.

2. Country Risk and Capacity to Service HG Loans

The determination of the eligibility of countries for market rate loans will be based on a case by case analysis of their debt servicing capabilities and an assessment of the prospects for timely repayment and of the risk of payment interruptions and consequent drain on HG reserves. The objective is to minimize the risk of lending to those countries which may soon be confronted with acute balance of payments and debt servicing problems. This analysis should be undertaken early in the project development process and any issues identified and re solved at the CDSS or OYB stage of project preparation. The analysis required is dynamic in nature. The level and rigor of analysis should be in line with generally accepted professional standards and with those followed by other U.S. Government agencies dealing with international loans. The time frame selected should be based on professional considerations. It should consider, among other factors, the volume of existing and projected debt, its costs, the time profile of servicing obligations, the economy's structural capacity to earn foreign exchange, past patterns and future prospects for economic growth and foreign trade, past management of external debt, and the effect of additional HG debt on its debt structure and debt service. The analysis should also assess whether a potential borrower is operating within an internal policy environment conducive to maintaining or improving its capacity to service external borrowing. USAID requires as a condition for its Housing Guaranty that the borrowing country either provide its sovereign guaranty or other acceptable guaranty to USAID to compensate USAID for any payments made to in investors. The sovereign guaranty of the borrowing country constitutes the maximum assurance USAID can have that HG loans will be repaid in dollars over the long-term.

3. HG Reserves Considerations

The HG loan program is not immune to the foreign debt servicing problems which many of the LDCs experience from time to time. The reason for applying credit worthiness standards to HG loans is to enhance the prospect of timely debt service performance and in this way minimize drawdowns of the reserve fund. As the HG loan from the private U.S. investors is protected 100% by the full faith and credit of the U.S. government, the investors look to the guaranty for the security of their investment and, therefore, perform no meaningful risk analysis on their own behalf. The purpose of the reserve fund is to provide for immediate compensation to the private U.S. investor for any delay in loan service receipts due. It therefore increases the attractiveness of HG loans as a media for investment.

A result of a series of non-performing HG loans (delinquencies, debt reschedulings, losses written off and in rare cases default) would be the ultimate depletion of the reserve fund and the inescapable requirement to ask Congress for appropriations to replenish it. Congress could be expected to take action to preserve the full faith and credit of the U.S. government guaranty backing outstanding HG obligations. However, there is no assurance that such action will result in a higher level of foreign assistance appropriations than would have been authorized in the absence of the necessity to accommodate the requirements of the HG program. Therefore, the accumulative result of non-performing HG loans and the requirement to make good the concomitant guaranties could result in unintended competition for new appropriations between HG loans authorized in the past and urgent current needs. Thus, the major difference between HG loans and ESF or DA loans is the risk that non-performing HG loans will result in the *a priori* attribution of precedence to the HG program over competing development programs, unplanned cuts in high priority items in our appropriations requests, and diminished control over allocations of FAA resources among countries and uses. These are the reasons more vigorous debt servicing capability analysis designed to identify risky countries is required for HG loans than for DA or ESF loans.

4. Ineligibility of Very Poor Countries

As a general principle, market rate HG loans are not an appropriate form of development assistance for very poor countries. Therefore, those countries which receive IDA credits, but not IBRD loans, will receive HG loans only after special justification is approved by Assistant Administrator of the Regional Bureau concerned and PPC, or the Administrator for the exceptional country.

Characteristically, these very poor countries, as defined above, have shallow resource bases and, consequently, slim prospects for improvement in their export earnings relative to their minimum import needs. In order not to jeopardize their long term development hopes, these countries must exercise caution in mortgaging their prospective export earnings. They must examine carefully both the terms of their foreign borrowings and the purposes for which such debts are incurred. The thirty year life and the ten year grace on principal repayments of the typical HG loan are advantageous, but the near commercial rate interest rate is not appropriate for the world's poorest countries. It is USAID's general policy to make all of its assistance to the Least Developed Countries in the form of grants if the availability of grant funds permits. In ranking competing needs for the small volume of nonconcessional foreign loans they can afford to service, priority must be given to financing the essential imports requirements of highly productive investments which will improve the economy's trade balance and its foreign debt servicing capabilities. Shelter projects require few imports (typically less than ten percent of the total cost). Hence they can be financed largely with local resources. They will not improve the debt servicing capability of the borrower. Therefore, shelter projects merit low priority in the competition for foreign loan resources.

Given these circumstances, a market rate HG loan to a very poor country can be justified only if the Mission concerned can demonstrate that the free dollars in excess of the requirement for imports for the shelter projects will be used in support of a sound investment program within the context of acceptable economic policies so that the benefits to the economy in terms of enhancement of its productive base and/or debt servicing capacity will exceed the cost of servicing the market rate HG loan over its life term. Alternatively, a HG loan may be justified if the Mission can demonstrate that the free dollars made available through the HG loans are programmed for investment in a specific set of priority productive projects which will yield high returns in increased production for exports or decreased import requirements, and that these benefits will exceed the cost of the HG loan.

VIII. ALLOCATION OF USAID's SHELTER SECTOR RESOURCES WITHIN THE RECIPIENT COUNTRY

It is clear that the magnitude of the shelter sector requirements in the LDCs far exceeds the level of resources available from USAID It is important, therefore, to utilize these technical and capital resources selectively to have the greatest impact.

1. Selection of Low-Income Target Groups

It is essential to direct USAID's programming at households below the median income. USAID's shelter program promotes equitable distribution of benefits in the shelter sector through increased access to land, shelter, infrastructure, and employment for the urban poor.

2. Selection of City and Town Locations For Shelter Sector Projects

We should seek to insure that neither shelter developments nor growth directing infrastructure (water and sewer systems as well as transportation arteries) take place or indirectly encourage building in hazard prone areas. Similarly, given the scarcity and productive value of agriculture and forest land in developing countries, our shelter and urban infrastructure interventions should seek to avoid the pre-emption of such lands for urban uses. Moreover, our shelter and urban infrastructure interventions should support higher urban density and greater infill development to the extent that they are viable options to outward urban expansion. So doing would avoid the risk of encroaching on valued agricultural and forest lands and, generally, would serve the interests of economic efficiency as, with high densities and less extensive infrastructure (shorter water and sewer trunklines, etc.), a greater number of inhabitants can benefit from a given unit of infrastructure.

Appendix I gives details on the implementation of HG projects.

APPENDIX I

IMPLEMENTATION OF THE HOUSING GUARANTY PROGRAM

The Housing Guaranty Program involves collaboration between the USAID Mission and a host country housing institution, such as a government ministry, a national housing bank or housing development corporation, a central savings and loan system, a national cooperative organization, or a similar institution in the private sector acting as borrower.

Following a request from the country and the USAID Mission, the Office of Housing and Urban Programs, working with host country officials, will prepare a shelter sector assessment. Based on this analysis, the office and the borrower determine the type of housing program to be financed and the institutional context within which it will be undertaken.

The major areas of concern to both parties at this stage are: (1) the progress which has been made towards the development of a rational shelter policy; (2) the contribution which the program will make towards the creation or strengthening of institutions needed to meet national shelter needs, especially the needs of the poor; (3) the establishment of roles for public and private sector involvement in shelter programs; (4) the capacity of the construction industry to supply housing over a given period; (5) the effective demand for housing at the agreed upon price level; and (6) the ability of the beneficiaries to repay their loans and the ability of the economy to make the dollar repayment.

When a mutually agreeable project has been developed and authorized by the Regional Bureau, the Office of Housing and Urban Programs and the borrower enter into an Implementation Agreement defining the use of the loan. Disbursements under the loan will be subject to the fulfillment of certain conditions as set forth in this agreement.

At the same time, the borrower seeks the most favorable terms available in the U.S. capital markets for a U.S. Government guaranteed loan. A typical Housing Guaranty loan is a long-term loan for a period of up to 30 years with a 10-year grace period on the repayment of the principal.

The U.S. lender and the borrower then negotiate the terms of the financing including interest rates which reflect the prevailing interest rates for similar maturing U.S. Government debt. These understandings are formalized in a loan agreement between the borrower and the lender, which is subject to USAID approval. In addition, certain provisions with regard to the paying and transfer agent, terms and amortization, prepayment rights of the borrower, and lenders fees and other charges must be included in each loan agreement, or otherwise agreed upon in a manner satisfactory to the Office of Housing and Urban Programs.

The USAID Guaranty

USAID will sign a contract of guaranty upon the signing of a loan agreement, indicating that repayment is guaranteed by the full faith and credit of the U.S. Government. The fees that USAID charges for its guaranty are as follows: 1) a fee of one-half of one percent (1/2%) per annum of the unpaid principal balance of the guaranteed loan; and 2) an initial charge of one percent (1%) of the amount of the loan, which is deducted from the loan disbursements. Additionally, USAID requires that the government of the borrowing country sign a full faith and credit guaranty of repayment of the loan and outstanding interest.

Lenders

A variety of participants in the U.S. capital markets, including investment bankers, commercial bankers, Federal Home Loan Banks, savings institutions, life insurance companies, and pension funds, have lent funds to host country borrowers as part of the Housing Guaranty Program. To be eligible to participate, lenders must be: 1) U.S. citizens; 2) domestic U.S. corporations, partnerships or associates substantially beneficially owned by U.S. citizens; 3) foreign corporations whose share capital is at least 95 percent owned by U.S. citizens; or 4) foreign partnerships or associations wholly owned by U.S. citizens.

Lender Selection

Lenders are selected by host country borrowers. The Office of Housing and Urban Programs encourages maximum contact between borrowers and lenders to facilitate loan arrangements that will best meet project needs, and to establish long-term borrower lender relationships to their mutual advantage. Lenders are typically selected through competitive negotiation process in which the Office of Housing and Urban Programs re quires that lending opportunities be advertise and that borrowers solicit lending proposals

A notice of each USAID guaranteed investment opportunity is published in the Federal Register. Notices are also mailed to interested individuals.

In certain circumstances and with the written consent of the Office of Housing and Urban Programs, lenders may be selected through noncompetitive negotiated process.

USAID Policy Papers and Policy Determinations

The following reports have been issued in a series. These documents with an identification code (e.g. PN-AAM-323) may be ordered in microfiche or paper copy. Please direct inquiries regarding orders to:

USAID Document and Information Handling Facility
7222 47th Street
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Title—Policy Paper	Date	Fiche #
Bureau for Private Enterprise	May 1982	PN-AAM-325
Domestic Water and Sanitation	May 1982	PN-AAM-323
Food and Agricultural Development	May 1982	PN-AAM-322
Nutrition	May 1982	PN-AAM-321
Private Enterprise Development	May 1982	PN-AAM-324
Recurrent Costs	May 1982	PN-AAM-319
Population Assistance	September 1982	PN-AAM-320
Private and Voluntary Organizations	September 1982	PN-AAM-318
Women in Development	October 1982	PN-AAL-777
Pricing, Subsidies, and Related Policies in Food and Agriculture	November 1982	PN-AAN-373
Approaches to the Policy Dialogue	December 1982	PN-AAM-431
Basic Education and Technical Training	December 1982	PN-AAM-190
Health Assistance	December 1982	PN-AAL-817
Institutional Development	March 1983	PN-AAN-108
Co-Financing	May 1983	PN-AAN-457
Local Organizations in Development	March 1984	PN-AAQ-157
Urban Development Policy	June 1984	PN-AAQ-158
Energy	July 1984	PN-AAQ-160
Shelter	February 1985	PN-AAQ-162

Title—Policy Determination	Date	Fiche #
PD #1—Narcotics	August 5, 1982	PN-AAM-443
PD #2—Mixed Credits	September 29, 1982	PN-AAM-444
PD #3—Voluntary Sterilization	September 1982	PN-AAM-445
PD #4—Title XII	October 5, 1982	PN-AAM-446
PD #5—Programming PL 480 Local Currency Generations	February 22, 1983	PN-AAM-591
PD #6—Environmental and Natural Resources Aspects of Development Assistance	April 26, 1983	PN-AAN-375
PD #7—Forestry Policy and Programs	May 16, 1983	PN-AAN-376
PD #8—Participant Training	July 13, 1983	PN-AAP-273
PD #9—Loan Terms Under PL 480 Title I	September 27, 1983	PN-AAN-753
PD #10—Development Communications	February 17, 1984	PN-AAP-616
PD #11—Using PL 480 Title II Food Aid for Emergency or Refugee Relief	July 26, 1984	PN-AAQ-159
PD #12—Human Rights	September 26, 1984	PN-AAQ-161